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No. 02-1581

In the Supreme Court of the United States

FORD T. JOHNSON, JR., PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTION PRESENTED

Whether petitioner "willfully" failed to pay over to the United States the payroll taxes withheld by his company from the wages of its employees and is therefore personally liable for the amount of those taxes under Section 6672 of the Internal Revenue Code, 26 U.S.C. 6672.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1-2) is not published in the *Federal Reporter* but is *reprinted in* 50 Fed. Appx. 113. The opinion of the district court (Pet. App. 5-25) is reported at 203 F. Supp. 2d 416.

JURISDICTION

The judgment of the court of appeals was entered on November 6, 2002. The petition for rehearing was denied on January 28, 2003. Pet. App. 26. The petition for a writ of certiorari was filed on April 28, 2003. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioner was the president, chairman of the board, founder and majority shareholder of a consulting company named Koba Associates, Inc. In those capacities, he was actively involved in the day-to-day management of the company and made all major decisions for it. In particular, he hired and supervised key employees and exercised control over the company's financial affairs. He had check signing authority on the company's bank account and routinely determined which creditors would be paid and how much to pay them. Pet. App. 8.

Throughout the period prior to and including 1994, petitioner's company experienced ongoing financial difficulties. The company was frequently delinquent in paying over to the government the taxes that it withheld from its employees' wages. Pet. App. 9. Petitioner testified, however, that, until these problems became severe during 1994, he "was always able to juggle it." *Ibid.* During 1994, as the company's financial situation worsened, petitioner hired Laurence Morrison as director of finance. *Ibid.* After hiring him, petitioner closely supervised Morrison and instructed him concerning his strategy for juggling payments among creditors and withholding taxes. *Id.* at 10. During the third quarter of 1994, petitioner promoted Morrison to vice president and met with Morrison weekly concerning financial matters. At those meetings, Morrison provided petitioner with lists of the company's accounts payable and with an accounting of the checks that had been written on the corporate accounts. *Ibid.*

2. In October 1994, petitioner reviewed and signed the company's quarterly tax return for the third

quarter of 1994. That return indicated that the company had unpaid withholding taxes due in the amount of $415,853.82 and that no payments had been made by the company for that quarter. Pet. App. 10. In that same month, petitioner was notified by the Internal Revenue Service (IRS) that the company was delinquent on its withholding taxes for the third quarter of 1994. After receiving that notice, petitioner contacted the IRS and agreed to a payment plan to satisfy the outstanding liability. Petitioner supervised his company's compliance with the payment plan at first but thereafter left Morrison in charge of financial matters. *Id.* at 11. Although Morrison regularly provided financial reports to petitioner during this period, those reports did not describe the status of the company's withholding tax obligations. *Id.* at 12.

3. The company continued to fail to pay employee withholding taxes during the fourth quarter of 1994 and stopped complying with the payment plan for the prior delinquencies. In December 1994, the IRS sent a notice of intent to levy to collect the unpaid taxes from the company. Pet. App. 12. Petitioner reviewed and signed the quarterly tax return for the fourth quarter of 1994, which indicated that the company had unpaid payroll taxes of $324,655.65. *Ibid.*

After receiving the notice of intent to levy, petitioner again briefly became involved in the company's employment tax situation. Petitioner again contacted the IRS and agreed to a second payment plan. Petitioner assigned Sandra Robinson, an in-house lawyer for the company, to supervise compliance with the second plan. Pet. App. 12. The company nonetheless again failed to comply with the new plan and did not meet its tax obligations for the first quarter of 1995. Petitioner reviewed and signed the tax return for the first quarter

of 1995, which clearly set forth the growing amount of the company's unpaid withholding tax liability. *Id.* at 12-13. Notwithstanding the substantial unpaid liability to the United States that existed throughout this period, the company continued to pay creditors other than the United States by "juggl[ing]" the funds obtained through the withheld taxes. *Id.* at 9, 13.

3. Under Section 6672(a) of the Internal Revenue Code, 26 U.S.C. 6672(a), a person who is responsible for paying over taxes withheld from employee wages but who "willfully" fails to do so is personally liable for the amount of taxes not paid over. Petitioner was assessed under this statute for the third and fourth quarters of 1994 and the first quarter of 1995. Pet. App. 7. When an overpayment of his personal income taxes was applied against this liability, petitioner filed suit in district court for a refund. The government counterclaimed for the balance of the unpaid assessment.

The district court granted summary judgment to the government. Pet. App. 5. The court held that petitioner had complete decision-making authority for the company and was therefore "responsible" as a matter of law for collecting and paying over the taxes withheld from the wages of the company's employees. *Id.* at 18-19. The court then further concluded, on the basis of the undisputed facts, that petitioner had acted "willfully" in failing to pay over those taxes and was therefore personally liable for the taxes under Section 6672(a). *Id.* at 19-20.

The court noted that petitioner was "an extremely well educated businessman," that he had "negotiated his company through delinquency problems with the IRS on a number of occasions," and that he "admittedly knew of the importance of honoring the obligation to pay withholding taxes." Pet. App. 19-20. The court

further noted that petitioner "knew of his company's tendency to fall behind on payroll taxes" and had selected Morrison "to manage this recurring problem." *Id.* at 20. After hiring Morrison in 1994, however, petitioner "made little effort to ensure that his new vice president was managing Koba's often-problematic payroll taxes." *Ibid.* In particular, although petitioner knew of the withholding tax delinquencies and had negotiated a payment plan with the IRS, petitioner failed to ensure that the plan was followed. *Ibid.* Instead, petitioner "withdrew his supervision and turned the plan over to Morrison, who, [petitioner] believed, had caused the deficiency in the first place." *Id.* at 21. Moreover, by the fourth quarter of 1994, although petitioner had actual knowledge that the company was "severely delinquent" in paying over its withheld payroll taxes, "at no time did [petitioner]: (1) request documentation that indicated that Morrison was paying the taxes; (2) contact the IRS to ensure that it was satisfied with Koba's compliance with the plan; (3) fire and replace Morrison for having neglected to pay the taxes in the first place; or (4) simply write checks on Koba's behalf to ensure compliance with the plan." *Ibid.* And, this same situation continued in the first quarter of 1995. *Id.* at 22. The court concluded that (*id.* at 23):

> [Petitioner] had actual knowledge of Koba's tax problems, and he directly involved himself in solving those problems by personally arranging two payment plans with the IRS. [Petitioner] then attempted to delegate the duty to comply with the plans to the very man who had caused the deficiency and failed to supervise him adequately under both plans. As an experienced businessman with knowl-

> edge of Koba's history of deficient taxes and the seriousness of honoring tax obligations, [petitioner] was, as a matter of law, willful in his failure to pay withholding taxes under section 6672.

4. In a brief *per curiam* opinion, the court of appeals affirmed "on the reasoning of the district court." Pet. App. 2. The court held that "[t]he evidence before the district court established that [petitioner] 'willfully' failed to pay over the payroll taxes at issue, within the meaning of § 6672." *Ibid.*

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or any other court of appeals. Further review is therefore not warranted.

1. a. Sections 3102(a) and 3402(a) of the Internal Revenue Code require employers to withhold taxes from the wages of their employees and to remit the amounts withheld to the government. 26 U.S.C. 3102(a), 3402(a). The taxes withheld by an employer from employee wages constitute a special trust fund for the benefit of the United States. 26 U.S.C. 7501; see *Begier* v. *IRS*, 496 U.S. 53, 60 (1990). A person who is responsible for collecting, accounting for, or paying over such trust fund withholding taxes—and who "willfully" fails to do so—is personally liable for the amount of those taxes under Section 6672(a) of the Code, 26 U.S.C. 6672(a). See *Slodov* v. *United States*, 436 U.S. 238, 242-245 (1978).

In the present case, there was no genuine dispute that petitioner was a "responsible person," who had the duty and authority to pay over his company's withholding taxes. The issue addressed by the parties was

whether petitioner's failure to pay over the withheld taxes to the government was "willful."

Willfulness under Section 6672 does not require an evil motive or an intent to deprive the government of revenue. See *e.g.*, *United States* v. *Rem*, 38 F.3d 634, 643 (2d Cir. 1994); *Kalb* v. *United States*, 505 F.2d 506, 511 (2d Cir. 1974), cert. denied, 421 U.S. 979 (1975). "A responsible person's intentional preference of other creditors over the United States establishes the element of willfulness under § 6672(a)." *Plett* v. *United States*, 185 F.3d 216, 219 (4th Cir. 1999); see *Phillips* v. *United States*, 73 F.3d 939, 942-943 (9th Cir. 1996). The failure of a person responsible for paying over trust fund taxes to the government is "willful" if he had actual knowledge that the taxes were not being paid or acted in reckless disregard of whether the payments were being made. *Plett* v. *United States*, 185 F.3d at 219; *United States* v. *Kim*, 111 F.3d 1351, 1357 (7th Cir. 1997). If the responsible person knew, or should have known, that trust fund taxes were not being remitted, but nevertheless acquiesced in preferring other creditors to the government, "willfulness" is established as a matter of law. *Plett* v. *United States*, 185 F.3d at 223; *Keller* v. *United States*, 46 F.3d 851, 855 (8th Cir.), cert. denied, 516 U.S. 824 (1995); *Jenson* v. *United States*, 23 F.3d 1393, 1395 (8th Cir. 1994); *Purcell* v. *United States*, 1 F.3d 932, 938 (9th Cir. 1993).

b. The courts below correctly held (Pet. App. 2, 23) that the evidence in this case established, as a matter of law, that petitioner acted "willfully" in failing to remit the withheld taxes to the government. In particular, the record conclusively established that petitioner was well aware that withheld taxes were being used to pay other creditors of the company and were not being paid over to the government. *Id.* at 9, 13.

For each period at issue, petitioner reviewed the company's tax returns, which plainly showed that withheld taxes had not been paid over to the government. Pet. App. 10, 12-13. Petitioner received regular accountings of checks written on behalf of the company, which also showed that taxes were not being paid over to the government. *Id.* at 20. Indeed, petitioner now acknowledges (Pet. 3) that he had actual knowledge that the withheld taxes were not being paid over to the government.

The record also clearly established that petitioner knew that amounts owed to other creditors were being paid during the same periods that the withheld taxes were not being paid to the government. Pet. App. 10, 13. This knowing use of trust fund withheld taxes to pay other creditors establishes that petitioner acted "willfully" as a matter of law. *E.g.*, *Plett* v. *United States*, 185 F.3d at 223; *Keller* v. *United States*, 46 F.3d at 855.

2. Petitioner argues that a conflict exists among the circuits because the Tenth Circuit has held that "reasonable cause" may justify an exception to liability that other courts have held exists under Section 6672 as a matter of law. Pet. 6-7 (citing *Finley* v. *United States*, 123 F.3d 1342, 1348 (10th Cir. 1997)). Since there is no plausible basis for petitioner to urge that he had "reasonable cause" for failing to pay over the withheld taxes, and since neither the district court nor the court of appeals addressed any such claim in this case, the decision below cannot be said to conflict with the reasoning or result in *Finley*.

Even if a "reasonable cause" exception to liability exists under Section 6672, it is clear that "reasonable cause" did not exist in this case. The courts that have described a "reasonable cause" exception to liability

under Section 6672 have emphasized that its application would necessarily be "exceedingly limited."[1] *Logal* v. *United States*, 195 F.3d 229, 233 (5th Cir. 1999). For example, in *Finley*, the Tenth Circuit stated that "reasonable cause sufficient to excuse a responsible person's failure to pay withholding taxes should be limited to those circumstances where (1) the taxpayer has made reasonable efforts to protect the trust funds, but (2) those efforts have been frustrated by circumstances outside the taxpayer's control." 123 F.3d at 1348. See also *Howell* v. *United States*, 164 F.3d 523, 526 (10th Cir. 1998) (same).[2]

In the present case, it is undisputed that petitioner had complete control over the finances of his company and could have taken action to see that the taxes were paid with available funds. Pet. App. 8. Even though he had actual knowledge that the withheld taxes were being misused to pay other creditors, petitioner did not take the ordinary step of simply writing a check to the government to pay the withheld taxes when due. *Id.* at

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[1] The First, Seventh, Eighth, and Ninth Circuits have declined to recognize a "reasonable cause" exception. *Olsen* v. *United States*, 952 F.2d 236, 241 (8th Cir. 1991); *Harrington* v. *United States*, 504 F.2d 1306, 1316 (1st Cir. 1974); *Pacific Nat'l Ins. Co.* v. *United States*, 422 F.2d 26, 33 & n.19 (9th Cir.), cert. denied, 398 U.S. 937 (1970); *Monday* v. *United States*, 421 F.2d 1210, 1216 (7th Cir.), cert. denied, 400 U.S. 821 (1970).

[2] In *Winter* v. *United States*, 196 F.3d 339 (2d Cir. 1999), the court of appeals merged the "willfulness" and "reasonable cause" inquiries by describing a "reasonable cause" exception from liability that exists when the responsible person held a "reasonable" belief that the taxes had in fact been properly paid over to the government. *Id.* at 345. In the present case, there is no dispute that petitioner had actual knowledge that the withheld taxes had not been paid over; petitioner thus plainly lacked any "reasonable" belief that the taxes had been paid.

21. Instead, he allowed other creditors to be paid with the trust funds withheld from employees' wages for the benefit of the United States. *Id.* at 13.

On this record, petitioner plainly did not make reasonable efforts to protect the trust fund taxes.[3] Even if a "reasonable cause" exception to liability exists, "[n]o such defense may be asserted by a responsible person who knew that the withholding taxes were due, but who made a conscious decision to use corporate funds to pay creditors other than the government." *Logal* v. *United States*, 195 F.3d at 232-233. Accord, *Thosteson* v. *United States*, 304 F.3d 1312, 1318-1320 (11th Cir. 2002). See also *Winter* v. *United States*, 196 F.3d at 345-346 (even if a "reasonable cause" exception to liability exists, and "even if a responsible person did not know contemporaneously of the company's nonpayment of withholding taxes, he or she will be held liable for any nonpayment if, when he or she became aware of the delinquency, the company had liquid assets with which to pay the overdue taxes").

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[3] This case is thus obviously distinguishable from *Finley*, 123 F.3d at 1344, where the responsible person delivered funds to his bank and directed that they be applied to withholding taxes, but the bank refused to do so. It is also distinguishable from *Howell*, 164 F.3d at 526-527, where the company set aside money to ensure that trust fund taxes were paid but its underwriters seized control of company and improperly used its accounts to pay other creditors.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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